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In the Supreme Court

OF THE

United States

OCTOBER TERM, 1981

R. E. LINDQUIST, ROBERT W. BLASCHKA, NORMAN D. MCPHAIL, ROY T. DRISCOLL, JOHN MOORE,
Petitioners,

VS.

CHARLES A. FOWLER,
Respondent.

PETITION FOR WRIT OF CERTIORARI
To the United States Court of Appeals
For the Ninth Circuit

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A. QUESTIONS PRESENTED FOR REVIEW

1. Whether or not the decision of the Court of Appeals conflicts with applicable decisions of this Court in reversing the conditional order of the Trial Court for new trial without holding that it was an abuse of discretion for the Trial Court to have found that the verdict was contrary to the clear weight of the evidence.

2. Whether or not this Court should settle the law concerning the Trial Court's instruction, upheld on appeal, that recklessness constitutes the necessary *scienter* to prove a violation of Section 10b of the Exchange Act and Rule 10b-5 thereunder.

3. Whether or not this Court should settle the law and resolve a conflict between circuits concerning the holding of the Court of Appeals that the defendant purchasers were controlling persons within the meaning of Title 15 U.S.C. Section 78t (Section 20(a) of the Exchange Act) even though the evidence would not justify a finding that they were culpable as required under holdings of the Courts of Appeals for the Second and Third Circuits.

B. LIST OF PARTIES

The caption of the case contains the names of all parties to the proceeding in the Court of Appeals for the Ninth Circuit. Defendant Bearing Specialty Co. was dismissed by plaintiff in the Trial Court and was not a party to the appeal.

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3. Whether or not this Court should settle the law and resolve a conflict between circuits concerning the holding of the Court of Appeals that the defendant purchasers were controlling persons within the meaning of Title 15 U.S.C. Section 78t (Section 20(a) of the Exchange Act) even though the evidence would not justify a finding that they were culpable as required under holdings of the Courts of Appeals for the Second and Third Circuits.

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D. REPORTS OF OPINIONS BELOW

None of the opinions below has been reported. The Appendix contains the opinion of the District Court granting judgment notwithstanding the verdict and conditionally ordering new trial (Appendix A), the opinion of the Court of Appeals for the Ninth Circuit reversing both orders (Appendix B) and the opinion of the Court of Appeals for the Ninth Circuit denying petition for rehearing (Appendix C). The Appendix also contains the petition for

rehearing (Appendix D), which shows that the Court of Appeals was presented specifically with the issue set forth as question 1 above.

E. GROUNDS ON WHICH JURISDICTION OF THE COURT IS INVOKED

(i) The Judgment of the Court of Appeals for the Ninth Circuit sought to be reviewed is dated and was entered January 22, 1982.

(ii) The order of the Court of Appeals for the Ninth Circuit denying rehearing is dated March 1, 1982.

(iii) This Court has jurisdiction to review the judgment by writ of certiorari under authority of Title 28 U.S.C. § 1254(1).

F. STATUTES AND REGULATIONS INVOLVED IN THE PETITION FOR CERTIORARI

The District Court had discretion to grant the conditional order for new trial under the authority of Rule 50(c)(1) of the Federal Rules of Civil Procedure, which reads as follows:

> "(c) Same: Conditional Rulings on Grant of Motion. (1) If the motion for judgment notwithstanding the verdict, provided for in subdivision (b) of this rule, is granted, the court shall also rule on the motion for a new trial, if any, by determining whether it should be granted if the judgment is thereafter vacated or reversed, and shall specify the grounds for granting or denying the motion for the new trial. If the motion for a new trial is thus conditionally granted, the order thereon does not affect the finality of the judgment. In case the motion for a new trial has been conditionally

granted and the judgment is reversed on appeal, the new trial shall proceed unless the appellate court has otherwise ordered. In case the motion for a new trial has been conditionally denied, the appellee on appeal may assert error in that denial; and if the judgment is reversed on appeal, subsequent proceedings shall be in accordance with the order of the appellate court."

The statute and regulation involved in the issue whether reckless conduct constitutes a violation of Section 10b of the Exchange Act are Title 15 U.S.C. § 78j(b) (Section 10b) and Rule 10b-5 thereunder. They read as follows:

"§ 78j. Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

• • •

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

June 6, 1934, c. 404, Title I, § 10, 48 Stat. 891."

Rule 10b-5:

"Employment of Manipulative and Deceptive Devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(a) to employ any device, scheme, or artifice to defraud,

(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security."

The statute involved in the issue whether the four purchasers can be held liable as controlling persons regardless of culpability is 15 U.S.C. § 78t(a) (Section 20 of the Exchange Act):

"§ 78t Liability of controlling persons

(a) Every person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person is liable, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action."

G. STATEMENT OF THE CASE

1. Background of the action in the Trial Court, and contentions of the parties

Plaintiff charged defendant officers of Bearing Specialty Company with misrepresentations and omissions in violation of Section 10b of the Exchange Act and under the California law of deceit in connection with the purchase by

four of them of his stock in Bearing Specialty Co. He charged that prior to closing of the sale of stock to the four individuals, defendant Lindquist had failed to notify plaintiff that the company was engaging in negotiations for a merger. Defendants contended that there was no duty to keep plaintiff informed, because in January 1977 plaintiff had exercised an option to sell his stock to the corporation, thereby binding himself by bilateral contract to sell to the corporation. Defendants contended that subsequent negotiations eventually resulting in a contract to sell to the individuals rather than to the corporation were negotiations for a novation. Defendants contended that because plaintiff had bound himself previously to sell to the corporation, he was obligated to sell his stock at the price fixed by his option agreement regardless of whatever information he might later acquire. Therefore, defendants contended, plaintiff could not have been damaged by any failure to keep him informed of negotiations which eventually led to a merger and an increase in value of the stock.

At trial, plaintiff contended that he had not exercised his option to sell to the corporation. He further contended that his failure to comply with the provisions for time and method of exercise of the option would have made any such exercise ineffective.

The Court gave instructions that reckless conduct could constitute sufficient *scienter* for violation of Section 10b of the Exchange Act. The Court also instructed that the four purchasers could be liable as controlling persons without proof of culpability.

The jury rendered a general verdict for plaintiff. The Trial Judge then granted judgment nov and a conditional order for new trial.

2. Evidence upon which the Trial Judge relied in granting the conditional order for new trial on the ground that the verdict was contrary to the weight of the evidence

District Judge Albert C. Wollenberg ordered a conditional new trial on the ground—which constituted a factual finding—that the verdict was against the clear weight of the evidence (Appendix A., pp. 20-21). As we shall show, the Court of Appeals did not dispute this finding (*infra*, p. 17). The evidence on which the Trial Judge relied was the same as that upon which he had relied to grant judgment nov (Appendix A, pp. 20-21). The Trial Judge concluded that plaintiff's testimony, as well as other evidence, lend inescapably to the conclusion that he did, in fact, exercise a legally valid option (Appendix A, p. 13). The Trial Judge found that plaintiff's own testimony established that "he unequivocally offered his stock for sale" (Appendix A, p. 14). The Trial Court found that "Plaintiff admits, contrary to his counsel's assertions, that he did not add any conditions to the terms of the proposed sale." (Appendix A, p. 15). The Court relied further upon the subsequent conduct of the parties to substantiate the conclusion that plaintiff had exercised his option to sell to the corporation: immediately after the meeting, the company commenced monthly payments to plaintiff "thereby evidencing its ultimate obligation to purchase the stock" (Appendix A, p. 16). "Two weeks after the meeting, Mr.

Linquist informed plaintiff that he would not personally purchase the stock as he was entitled to do under the written agreement." (*ibid*). The Trial Court also relied upon discussions concerning the substitution of the parties and the method of computing the price as "additional indicators that the parties considered themselves bound by the terms of the agreement and that they believed they could only change those terms by gaining the consent of the other party." (*ibid*).

The Trial Judge dismissed testimony of plaintiff that in September 1977, Mr. Lindquist had told him that he could change his mind with respect to the sale of the stock; Judge Wollenberg concluded that this testimony, "carries little weight due to its inherent ambiguities, directly conflicts with plaintiff's other testimony, the vagueness of plaintiff's recollection, and the leading nature of counsel's question." (*id* at 17).

Although the fact is not mentioned in the Trial Judge's opinion, plaintiff was impeached many times during the trial.

3. The Appellate Court reversed the new trial order on the ground that "there is no valid useful purpose for submitting the case to another jury" without rejecting the Trial Court finding that the verdict was contrary to the clear weight of the evidence

The Court of Appeals reversed the judgment notwithstanding the verdict on the basis of plaintiff's testimony that Lindquist had subsequently assured plaintiff that he

could change his mind (Appendix B, pp. 25, 26). This is the same testimony which Judge Wollenberg had found to carry "little weight" (*supra*, p. 7). The Court of Appeals held that the jury could have reasonably found that although the company was bound to the option to purchase plaintiff's stock, a condition subsequent permitted plaintiff to cancel the agreement to purchase and sell if merger negotiations should occur prior to closing of the sale (Appendix B, p. 26). The Court of Appeals then reversed the conditional grant of a new trial, stating that the Court was convinced "that 'there is no valid useful purpose for submitting the case to another jury.' *Fireman's Fund Insurance Co. v. Aalco Wrecking Co.*, 466 F.2d 179, 187 (8th Cir. 1972)." (Appendix B, p. 28).

On motion for rehearing, petitioners called the Court's attention to the fact that the opinion had reversed the new trial order without rejecting Judge Wollenberg's finding that the verdict was against the clear weight of the evidence (Appendix D, p. 33). The Court of Appeals, however, denied rehearing without referring at all to the assertion that the finding had not been rejected (Appendix C).

4. The Trial Court instructed the jury that reckless action constitutes a violation of Section 10b-5 of the Exchange Act, and the Court of Appeals affirmed without discussion of the point raised on appeal

Instruction 24, read and handed to the jury by the Trial Court, defined the elements which must be proved to establish a violation of Section 10b-5 of the Exchange Act. One

element set forth in the instruction was, "That the defendant(s) acted knowingly or recklessly, as those terms are defined in these instructions." Instruction 25 repeated that plaintiff claimed knowing or reckless conduct. Instruction 26 included recklessness as an element of proof of a 10b-5 violation. Instructions 28 and 31 also mentioned reckless conduct as constituting a violation.

The point was raised on appeal to the Ninth Circuit, although the Circuit had already ruled that reckless conduct constitutes sufficient *scienter* for a violation of Rule 10b-5. The Court of Appeals opinion did not deal with the point (Appendix B).

5. The Trial Court instructed the jury that defendant purchasers could be controlling persons of Lindquist, the negotiator, without proof of culpability, and the Court of Appeals confirmed that this was a correct statement of the law

Instruction No. 30 given by the Trial Court stated that "all that must be shown" [to prove liability as a controlling person] "is that the controlling persons are the actual intended beneficiaries of the stock transaction and that they directly or indirectly induced the purchase." No proof of their culpability was required.

The Court of Appeals held that "the liability of appellees Driscoll, McPhail and Moore under the controlling person doctrine of the securities law is supported by the evidence." (Appendix B, p. 24).

H. NOT APPLICABLE

I. BASIS FOR FEDERAL JURISDICTION IN THE COURT OF FIRST INSTANCE

Count I of the action asserted jurisdiction under Section 27 of the Exchange Act of 1934, 15 U.S.C. Section 78aa, and 28 U.S.C. Section 1331. Counts II and III asserted pendent jurisdiction.

J. ARGUMENT

1. In holding that a new trial would serve no purpose, despite the Trial Judge's unchallenged finding that the jury verdict was contrary to the clear weight of the evidence, the Court of Appeals' reversal of the new trial order conflicts with long established doctrine of this Court

(a) This Court has consistently held that the power to grant a new trial rests almost entirely within the discretion of the trial judge

Because of the unique opportunity of the trial judge to observe the conduct of the proceedings, this Court has held that the grant of a new trial should almost never be reversed by a court of appeals.

In *Montgomery Ward & Co. v. Duncan*, 311 U.S. 243, 61 S.Ct. 189, 85 L.Ed. 147 (1940) the court modified a judgment of a court of appeals which had reversed a judgment nov and directed entry of judgment on the verdict, as the 9th Circuit did in this case.[1] This court modi-

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[1]In *Montgomery Ward*, however, the trial judge had not ruled on the alternative motion for new trial.

fied the judgment below to remand the case to the district court to consider whether or not the alternative motion for new trial should have been granted. In doing so, this court emphasized the importance of a ruling by the trial court. The court states (311 U.S. at 251): ". . . the party against whom the verdict went is entitled to have his motion considered in respect of asserted substantial trial errors and matters appealing to the discretion of the judge." The court added (311 U.S. at 254):

> "Should the trial judge enter judgment n.o.v. and, in the alternative, grant a new trial on any of the grounds assigned therefor, his disposition of the motion for a new trial would not ordinarily be reviewable and only his action in entering judgment would be ground of appeal."

In *Fairmount Glass Works v. Cub Fork Coal Co.*, 287 U.S. 474, 53 S.Ct. 252, 77 L.Ed. 439 (1933), the Court reversed an appellate court decision granting a new trial for failure of the jury to award substantial damages proved at trial where the trial court had denied new trial. This court treated the decision of the trial judge on new trial as one of fact which is never reversed on appeal except under certain specific circumstances not present here. The Court noted that this rule "has been settled by a long and unbroken line of decisions" stating (287 U.S. at 481):

> "The rule that this Court will not review the action of a federal trial court in granting or denying a motion for a new trial for error of fact has been settled by a long and unbroken line of decisions; and has been frequently applied where the ground of the motion was that the damages awarded by the jury were excessive or were inadequate. The rule precludes likewise a re-

> view of such action by a circuit court of appeals. Its early formulation by this Court was influenced by the mandate of the Judiciary Act of 1789, which provided in § 22 that there should be 'no reversal in either [circuit or Supreme] court on such writ of error . . . for any error in fact."

This Court noted that, as in this case, the appellate court had not found an abuse of discretion by the trial judge (287 U.S. at 485):

> "Third. It is urged that the refusal to set aside the verdict was an abuse of the trial court's decision, and hence reviewable. The Court of Appeals has not declared that the trial judge abused his discretion."

In *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 60 S.Ct. 811, 84 L.Ed. 1129 (1940) this Court relied upon *Fairmount Glass Works* to hold that there was no showing of abuse of discretion in the grant of motion for new trial for some defendants and denial as to others. The Court states (310 U.S. at 247):

> ". . . [T]his case falls within the well established rule that neither this Court nor the Circuit Court of Appeals will review the action of a federal trial court in granting or denying a motion for a new trial for error of fact, since much action is a matter within the discretion of the trial court. Fairmount Glass Works v. Cub Fork Coal Co. 287 US 474, 77 L ed 439, 53 S Ct 252. Certain exceptions have been noted, such as instances where the trial court has 'erroneously excluded from consideration matters which were appropriate to a decision on the motion.' Fairmount Glass Works v. Cub Fork Coal Co. supra (287 US 483, 77 L ed 444, 53 S Ct 252). But there are no such circumstances here.

• • •

Certainly, denial of a motion for a new trial on the grounds that the verdict was against the weight of the evidence would not be subject to review. Moore v. United States, 150 US 57, 61, 62, 37 L ed 996, 998, 14 S Ct 26; J. W. Bishop Co. v. Shelhorse (CCA 4th) 141 F 643, 648; O'Donnell v. New York Transp. Co. (CCA 2d) 187 F 109, 110. In substance no more than that is involved here."

Again in *United States v. Johnson*, 327 U.S. 106, 66 S.Ct. 464, 90 L.Ed. 562 (1946) which had been a criminal trial before a jury, this Court reversed an order of the appellate court which had itself reversed a trial court denial of new trial urged on the ground of newly discovered evidence proving perjury. The Court noted that the trial judge's decision on the evidence was one of fact which is not reviewable by the court of appeals or this Court (327 U.S. at 111):

"In our opinion the Circuit Court of Appeals erred. The appeal to that court was so devoid of merit that it should have been dismissed. The crucial question before the trial court was one of fact: Did the new evidence show that Goldstein's original testimony was false? The trial judge after carefully studying all the evidence found that there was nothing to show perjury on the part of Goldstein, that Goldstein had in fact told the truth, and concluded that a new trial was not warranted. But it is not the province of this Court or the Circuit Court of Appeals to review orders granting or denying motions for a new trial when such review is sought on the alleged ground that the trial court

made erroneous findings of fact. Holmgren v. United States, 217 US 509, 54 L ed 861, 30 S Ct 588, 19 Ann Cas 778; Holt v. United States, 218 US 245, 54 L ed 1021, 31 S Ct 2, 20 Ann Cas 1138; Fairmount Glass Works v. Cub Fork Coal Co., 287 US 474, 481, 77 L ed 439, 443, 53 S Ct. 252. While the appellate court might intervene when the findings of fact are wholly unsupported by evidence, cf. United States v. Socony-Vacuum Oil Co., 310 US 150, 247, 84 L ed 1129, 1180, 60 S Ct 811; Glasser v. United States, 315 US 60, 87, 86 L ed 680, 708, 62 S Ct 457, it should never do so where it does not clearly appear that the findings are not supported by any evidence.

The trial judge's findings were supported by evidence. He had conducted the original trial and had watched the case against Johnson and the other respondents unfold from day to day. Consequently the trial judge was exceptionally qualified to pass on the affidavits The record of both the original trial and the proceedings on the motions for a new trial shows clearly that the trial judge gave the numerous elements of the controversy careful and honest consideration. We think that even a casual perusal of this record should have revealed to the Circuit Court of Appeals that here nothing more was involved than an effort to upset a trial court's findings of fact."

The unique insight of the trial judge was again emphasized in *Cone v. West Virginia Pulp & P. Co.*, 330 U.S. 212, 67 S.Ct. 752, 91 L.Ed. 849 (1947). The trial court had denied a directed verdict and the jury then returned a verdict for the other party. No motion for judgment nov was made, although a motion for new trial on the ground of newly discovered evidence was made by the losing

party and denied by the trial court. The court of appeals reversed on the ground that an essential element of proof was missing and, instead of remanding for a new trial, directed entry of judgment for the opposite party (a judgment notwithstanding the verdict). This Court reversed, and emphasized at length the importance, in making a decision whether or not to grant a new trial, of the insight of the trial judge into the issues involved, the kind of evidence given and the impression made by witnesses (300 U.S. at 216):

> ". . . [H]e can see (sic) exercise this discretion with a fresh personal knowledge of the issues involved, the kind of evidence given, and the impression made by witnesses. His appraisal of the bona fides of the claims asserted by the litigants is of great value in reaching a conclusion as to whether a new trial should be granted. Determination of whether a new trial should be granted or a judgment entered under Rule 50(b) calls for the judgment in the first instance of the judge who saw and heard the witnesses and has the feel of the case which no appellate printed transcript can impart."

This Court applied and extended the ruling of *Cone* in *Globe Liquor Co. v. San Roman*, 332 U.S. 571, 68 S.Ct. 246, 92 L.Ed. 177 (1948). The Court at 332 U.S. 574 quoted from the *Cone* opinion to emphasize the trial judge is the one " 'who saw and heard the witnesses and has the feel of the case which no appellate printed transcript can impart.' "

In *Neely v. Eby Construction Company*, 386 U.S. 317, 325, 87 S.Ct. 1072, 1078, 18 L.Ed.2d 75, 82 (1967) the Court

affirmed the action of a court of appeals in directing judgment nov where the verdict-winner appellee had failed to ask the appellate court for new trial under Rule 50(b). In doing so, the Court discussed the rationale of the *Cone* and *Globe Liquor* cases and instructed that a court of appeals "should be constantly alert" to the superior knowledge of new trial issues which only the trial judge possesses. The Court referred to "the trial judge's first-hand knowledge of witnesses, testimony and issues—his 'feel' for the overall case" (336 U.S. at 325).

The most recent affirmation of the doctrine of deference to the trial court's findings of fact in granting new trial is in *Allied Chemical Corp. v. Daiflon, Inc.*, 449 U.S. 33, 101 S.Ct. 188, 66 L.Ed.2d 193 (1980). In *Allied Chemical* the Court reversed a writ of mandamus which had directed the trial court to restore in part a jury verdict after the trial court had granted new trial. In holding that the right to mandamus could not be clear and indisputable, the court noted the broad discretion of the trial court in ruling on new trial (449 U.S. at 36):

> "The authority to grant a new trial, moreover, is confined almost entirely to the exercise of discretion on the part of the trial court. Where a matter is committed to discretion, it cannot be said that a litigant's right to a particular result is 'clear and indisputable.'"

(b) The Court of Appeals reversed the Trial Judge's new trial order without holding that he abused his discretion in finding that the verdict was against the clear weight of the evidence

As noted, the only comment of the Court of Appeals in reversing the new trial order was to state that the Court was convinced that there is no valid useful purpose for submitting the case to another jury, citing *Fireman's Fund Insurance Co. v. Aalco Wrecking Co.*, 466 F.2d 179, 187 (8th Cir. 1972) (cert. den. 410 U.S. 930) (Appendix B, p. 28). By petition for rehearing, defendants argued to the court of appeals that its ruling departed from the doctrine cited above of deference to the findings of the trial judge on new trial (Appendix D, p. 32). However, rehearing was denied without comment, and again without reference to the finding of the trial judge that the verdict was against the clear weight of the evidence (Appendix C).

The *Fireman's Fund* case cited by the Appellate Court was an Eighth Circuit opinion which had reversed a district court judgment nov and conditional order of new trial, directing judgment for plaintiffs in accordance with the original verdict. The *Fireman's Fund* opinion applied to review of a new trial order the standard which has been used traditionally in reviewing judgment nov: whether "reasonable men may differ as to the result" (466 F.2d at 187). The court in *Fireman's Fund* relied upon *Lind v.*

Schenley Industries, 278 F.2d 79 (3d Cir. 1960) (cert. den. 364 U.S. 835) stating (466 F.2d at 187):

> "It has been recognized in the *Lind* case, supra, that where the trial court finds the verdict contrary to the weight of the evidence and grants a new trial that the appellate court should 'exercise a closer degree of scrutiny and supervision . . . in order to protect the litigants' right to jury trial.' 278 F.2d at 90."

A petition for rehearing en banc was denied in *Fireman's Fund*, but Judge Mehaffy, joined by Chief Judge Matthes, dissented, pointing out that the reversal of the new trial order "ignores the teachings of the Supreme Court in cases of this nature" (466 F.2d at 188). The dissenters argued that reversal is not justified without a finding of clear abuse of discretion, (*id* at 189) citing the *Fairmount*, *Socony-Vacuum*, *Johnson* and *Neely* cases which we have cited above.

Lind v. Schenley Industries, Inc., 278 F.2d 79, 90 (3d Cir. 1960) (cert. den. 364 U.S. 835) was cited extensively in plaintiff-appellant's brief in this case. Contrary to the consistent holdings of this Court, the Third Circuit in *Lind* held that when a trial judge grants a new trial on the ground that the verdict was against the weight of the evidence (278 F.2d at 90), ". . . the judge takes over, if he does not usurp, the prime function of the jury as the trier of the facts. It then becomes the duty of the appellate tribunal to exercise a closer degree of scrutiny and supervision than is the case where a new trial is granted because of some undesirable or pernicious influence obtruding into the trial."

The Third Circuit also declared in *Lind* (p. 90) ". . . that there is no consensus of opinion as to the exact standards to be used by a trial court in granting a new trial and that the criteria to be employed by an appellate tribunal charged with reviewing the trial judge's decision in this respect are equally indefinite."

A comment in 13 *Stanford Law Review* 383, 385 criticized the *Lind* decision as "without precedent." Yet the *Lind* heresy appears to have been followed in other circuits. See *Borras v. Sea-Land Service, Inc.*, 586 F.2d 881, 887 (1st Cir. 1978) (citing as "the modern trend" *Lind* and the *Fireman's Fund* decision cited by the Appellate Court in this case); *Vander Zee v. Karabatsos*, 589 F.2d 723, 729 (D.C. Cir. 1978) (cert. den. 442 U.S. 910). With the decision herein, it appears that the panel of the Ninth Circuit sitting below has also forsaken the long established rule which this Court has enunciated, and which the Ninth Circuit had followed to the date of this decision. (See *Fount-Wip, Inc. v. Reddi-Wip, Inc.*, 568 F.2d 1296, 1302 (9th Cir. 1978).)

We submit that this Court should seize this opportunity to reiterate its doctrine 1) that a trial judge has the power and duty to grant a new trial if he finds, as here, that a verdict is against the clear weight of the evidence, and 2) that an appellate court will rarely reverse the trial court's findings on grant or denial of a new trial.

2. This Court should settle the law as to whether or not reckless conduct constitutes the necessary scienter to prove a violation of Section 10b of the Exchange Act and Rule 10b-5 thereunder

In *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 96 S.Ct. 1375, 47 L.Ed.2d 668 (1976), the court ruled that liability under Section 10b and Rule 10b-5 could not be imposed for negligent conduct alone. The court expressly reserved the question of whether reckless behavior may be sufficient for civil liability (425 U.S. at 193, footnote 12). The Ninth Circuit has held that reckless conduct is sufficient, in *Nelson v. Serwold*, 576 F.2d 1332, 1337 (9th Cir. 1978) (cert. den. 439 U.S. 970). The decision in this case is also a holding to that effect, since defendants argued that the trial court had improperly instructed the jury that recklessness is sufficient. A number of other circuits have so ruled. In *Sanders v. John Nuveen & Co., Inc.*, 554 F.2d 790 (7th Cir. 1977) the Seventh Circuit adopted a modified rule that recklessness is sufficient which (p. 793) ". . . comes closer to a lesser form of intent than merely a greater degree of ordinary negligence."

It would be a great service to those who must act under the strictures of Section 10b and Rule 10b-5 and would produce a saving of untold sums spent in legal proceedings as well as a saving in judicial and lawyers' time if this Court would settle the law as to the character of the conduct which is necessary to establish *scienter*.

3. This Court should settle the law and resolve a conflict between circuits as to the holding that the defendant purchasers were controlling persons under Section 20(a) of the Exchange Act without proof of culpability

The Court of Appeals held that the liability of appellees Driscoll, McPhail and Moore under the controlling person doctrine was supported by the evidence (Appendix B, p. 24). The extent of their involvement with the negotiations was that they were buyers of plaintiff's stock, and that defendant Lindquist, their superior in the corporation, negotiated the purchase on their behalf.

Thus, without discussion, this panel of the Ninth Circuit has rejected the rule of the Second and Third Circuits that in order to be liable under the Exchange Act as a controlling person, one must be a culpable participant in the activities of the controlled person whose conduct is claimed to violate the securities laws.

After an exhaustive in banc analysis of legislative history, common law, English law and the case development of Rule 10b-5, the Second Circuit, in *Lanza v. Drexel*, 479 F.2d 1277 (2d Cir. 1973) adopted its rule that one must be culpable in order to be liable as a controlling person. The court held (p. 1299):

> "The intent of Congress in adding this section, passed at the same time as the amendment to Section 15 of the 1933 Act, was obviously to impose liability only on those directors who fall within its definition of control and who are in some meaningful sense culpable participants in the fraud perpetuated by controlled persons."

In *Gordon v. Burr*, 506 F.2d 1080, 1085 (2d Cir. 1974) the Second Circuit adhered to the rule.

In the well-known case of *Rochez Brothers, Inc. v. Rhoades*, 527 F.2d 880, 891 (3d Cir. 1975), the Third Circuit adopted the same rule requiring culpability. The court held that liability may be premised on inaction (p. 891), "only if it is apparent that the inaction intentionally furthered the fraud or prevented its discovery."

As both Second and Third Circuits have noted, the wording of Section 20 itself provides a defense against liability if the controlling person, "acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action."

In *Christoffel v. E. F. Hutton & Co., Inc.*, 588 F.2d 665, 668 (9th Cir. 1978) the Ninth Circuit expressly refrained from deciding the issue. Now in this case the Ninth Circuit has done so, without analysis of the authorities.

The extent of liability under the controlling person doctrine is another important aspect of the Securities laws which has not been settled by this Court. This case involves an uncluttered factual situation in which to render a decision on this important issue. The only evidence of the involvement of these buyers in the subject matter of the charges is that they authorized their superior, Lindquist, to negotiate for them and that they purchased the stock and thereby received the benefit of its subsequent increase in value. As would a decision whether recklessness constitutes sufficient *scienter* for violation of Section 10b, a decision defining the extent of liability under the con-

trolling person provisions of the Exchange Act would greatly aid those who must conform their conduct to the admonitions of the Securities Laws.

K. CONCLUSION

We ask this Court to grant certiorari in order to restore to the trial judge the traditional power and duty to grant a new trial when his trained perception leads him to conclude that a jury verdict is contrary to the clear weight of the evidence. In these days of complicated factual issues such as those presented under the Securities Act, this traditional power of the trial judge is more important than ever. The other two issues we have raised for consideration relate to important sections of the Securities Laws which raise daily problems for those who must do business under those laws, as well as for their advisors, and advocates. These are three important issues which cry for definitive determinations by this Court.

Dated: May 18, 1982

Respectfully submittted,
ACKERMAN, JOHNSTON, CAMPBELL & PARKINSON

By BENJAMIN H. PARKINSON
Counsel of Record for Petitioners R. E. Lindquist, Robert W. Blaschka, Norman D. McPhail, Roy T. Driscoll, and John Moore

(Appendices follow)

APPENDIX A

United States District Court
Northern District of California

No. C-78-1190 ACW

Charles A. Fowler,
Plaintiff,

vs.

Bearing Specialty Company, a corporation,
R. E. Lindquist, Robert W. Blaschka,
Norman D. McPhail, Roy T. Driscoll, and John Moore,
Defendants.

Judgment

[Filed June 11, 1980]

Defendants' motion for a judgment notwithstanding the verdict having come before the Court, Honorable Albert C. Wollenberg, District Judge, presiding, and the issues having been duly presented by the parties and the Court having concluded that the evidence presented at trial only supported a favorable verdict for defendants.

It Is Hereby Ordered and Adjudged that defendants' motion for a judgment notwithstanding the verdict is GRANTED, that the plaintiff take nothing, and that the defendants recover of the plaintiff their costs of action.

Dated: June 11, 1980.

/s/ ALBERT C. WOLLENBERG
United States District Judge

United States District Court
Northern District of California

No. C-78-1190 ACW

Charles A. Fowler,
Plaintiff,

vs.

Bearing Specialty Company, a corporation,
R. E. Lindquist, Robert W. Blaschka,
Norman D. McPhail, Roy T. Driscoll, and John Moore,
Defendants.

Order Granting Defendants' Motion for a
Judgment Notwithstanding the Verdict

[Filed June 11, 1980]

Plaintiff Charles A. Fowler brought this action against defendants Bearing Specialty Company ("Bearing") and its corporate officers Rudolph Lindquist, Robert Blaschka, Norman McPhail, Roy Driscoll, and John Moore. Fowler has alleged that defendants violated section 10b of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and various common law duties owed him under state law in connection with his sale to defendants Blaschka, McPhail, Driscoll, and Moore of about 22,000 shares of Bearing stock.

On seven days commencing on April 7, 1980, the case was tried before a jury. During the trial, the Court dismissed the claims against Bearing. The jury returned verdicts against the remaining defendants, finding that they

had all committed violations of the Securities Act and that Lindquist had also committed the tort of negligent misrepresentation. The jury awarded Fowler damages of $36,000 "plus plaintiff's attorney's fees and court costs" against Lindquist and the amount against the other defendants of $6.50 per share of stock which each of them had purchased from plaintiff. Upon the dismissal of the jury, defendants renewed their pending motions for a directed verdict in the form of a motion for a judgment notwithstanding the verdict and, in the alternative, a motion for a new trial. Plaintiff subsequently requested that the Court amend the verdict against defendant Lindquist. Having considered the oral and written arguments of counsel on these matters and having reviewed the entire record herein, the Court now grants defendants' motion for a judgment notwithstanding the verdict.

FACTS

The presentation of the evidence at the trial raised only a few significant factual disputes. This factor accounts for the narrative form of the following explication of that evidence.

In January 1973, plaintiff's company, the Charles A. Fowler Company, merged with Bearing, a company which defendant Lindquist owned and managed. Plaintiff received Bearing stock in exchange for his interest in his company. In addition, the parties to the transaction entered into a written agreement under the terms of which Bearing promised to employ plaintiff for a four-year term, with an option to renew or terminate his employment at the end of that time. The agreement also provided plaintiff or his

personal representative with a means of disposing of his Bearing stock in the event of his death, total disability, or the termination of his employment. Upon the occurrence of any of those circumstances, plaintiff or his personal representative had the right to retain his stock or to exercise an option to sell his stock to the corporation at book value, to be paid in installments together with interest on the unpaid balance at the annual rate of six percent. The option to sell was to be exercised in writing and within 20 days of the occurrence giving rise to the option if that event was the termination of plaintiff's employment. Lindquist, acting in a personal capacity, had the right of first refusal, but upon his failure to exercise this right the corporation remained obligated to purchase the stock.

On December 31, 1976, after the completion of his four-year term of employment, Fowler's employment with Bearing was terminated. He immediately departed on a vacation to Hawaii which Bearing and some of its suppliers had provided for him. Shortly after his return, Lindquist contacted him by telephone and arranged a meeting for the purpose of discussing what Fowler intended to do with his Bearing stock. Pursuant to this conversation, on January 27, 1977, Fowler met with Lindquist and Blaschka at Bearing's offices.

The parties' different characterizations of what events transpired at this meeting gives rise to the most important factual and legal disputes of the case. The parties agree that their discussion focused upon plaintiff's intentions regarding his Bearing stock. Plaintiff acknowledges that he expressed a willingness to sell his stock to the corpora-

tion, but he argues that he conditioned this offer upon his right to retain the stock if Bearing engaged in any serious merger negotiations prior to the finalization of the transaction. Plaintiff denies that he exercised the option found in the written agreement; rather, he contends that his statements at the meeting constituted a counteroffer which defendants did not accept until the signing of the written agreement on November 4, 1977. Defendants Lindquist and Blaschka testified that at this meeting, plaintiff clearly and unequivocally stated his desire to sell his stock to the corporation pursuant to the terms of the written agreement. They understood him to be exercising his option.

While the parties vigorously dispute the question of whether Fowler in fact exercised his option at this meeting, they are in substantial agreement concerning one event that then occurred. In the course of their conversation, Lindquist informed Fowler that Bearing was willing to commence payments to him of approximately $1,000 per month. Fowler accepted this offer. The payments began on January 28 and continued until the consummation of the sale. On some occasions, Fowler requested and received payments of $2,000. Fowler testified that he viewed the payments "as interest on what the approximate value of the shares of stock would be." Reporter's Excerpted Transcript [hereinafter "Transcript"], Cross-Examination of Charles A. Fowler at 20. Defendants stated that the payments represented "advances" on the money that Bearing would eventually transfer to Fowler in exchange for his stock. Some of the vouchers were marked with the notation "advance".

Throughout the rest of the year, the parties engaged in a series of meetings and communications in which they discussed particular elements of the proposed exchange. The participants in the January meeting met again on February 14. Defendants' uncontradicted testimony indicated that at this time Lindquist informed Fowler that he declined to exercise his right, as provided by the initial written agreement, to purchase the proffered stock. He questioned Fowler, however, as to whether he would consider selling the stock to company executives Blaschka, Driscoll, and McPhail as opposed to the corporation. (Defendant Moore's name was subsequently added to this group.) Two weeks later at another meeting, Fowler conditioned his acceptance of the substitution of the parties upon their willingness to pay an interest rate on the unpaid balance in excess of the annual six percent rate provided for in the written agreement. Lindquist and Blaschka, acting on behalf of these individuals at two meetings held in May and June, rejected plaintiff's offer.

In July, when Lindquist was on vacation, Fowler received a letter from Bearing's attorney concerning the price to be paid for the stock. The attorney asserted therein that the book value price specified in the written agreement contemplated calculating that sum with reference to the adjusted value of the stock in 1977 as opposed to 1973. Utilization of the 1977 value would have reduced the amount due plaintiff because of a change in the inventory valuation which had occurred subsequent to execution of the 1973 agreement. Plaintiff registered strenuous objections to this contract interpretation. At a meeting held with

Lindquist in August 1977, Lindquist agreed with Fowler's contentions regarding the price to be paid for the stock. Fowler, on his part, agreed at this meeting to the substitution of the individual purchasers for the corporation without the imposition of an additional interest charge.

Fowler also testified that Lindquist informed him at a September meeting that Bearing was not then engaged in any merger negotiations and that he may have told him that Fowler still retained the right to back out of the proposed sale. Transcript, Redirect Examination of Charles A. Fowler at 4. Lindquist denied making any such statement except at the January meeting and claimed that no September meeting occurred.

Upon Lindquist's return from another vacation, the parties met on November 4 and signed the documents finalizing the sale. This contract differed from the 1973 written agreement in two respects. First, individual executives of Bearing purchased the stock instead of the corporation. In addition, plaintiff withheld a portion of the stock for sale to his son rather than exchanging his entire share as contemplated by the agreement. Defendants had granted plaintiff's request for this latter deviation at some earlier stage of their discussions.

Approximately one month after the consummation of this sale, on December 1, 1977, Lindquist agreed to a merger offer made on behalf of the Genuine Parts Company. Plaintiff conceded at trial that the material events leading up to this merger occurred in 1977 after the January meeting. The relevant occurrences which preceded the finalization of plaintiff's sale of stock included an informal

discussion of merger between Lindquist and Genuine Parts' executives, the exchange of financial information between the companies, and an inspection visit of Bearing made by three top Genuine Parts' executives. Defendants failed to inform plaintiff of any of these events.

Plaintiff received $8.16 per share of stock that he sold. Upon the completion of the merger, in June 1978, the holders of Bearing stock exchanged their stock for an equal amount of stock in Genuine Parts worth $14.66 per share. If plaintiff had retained his stock, its value would have increased approximately $142,000 from its worth the day that he sold it.

STANDARD FOR DETERMINING A MOTION FOR A JUDGMENT NOTWITHSTANDING THE VERDICT

The same standard governs the determination of a motion for a judgment notwithstanding the verdict and a motion for a directed verdict. *Hallmark Industry v. Reynolds Metals Co.*, 489 F.2d 8, 13 (9th Cir. 1973), *cert. denied*, 417 U.S. 932 (1974). When considering such a motion, a court must take special care to avoid invading the factfinding province of a jury. It is not the reviewing court's function to weigh the evidence. That evidence must be viewed in the light most favorable to the nonmoving party and that party must be given the benefit of all the reasonable inferences which can be drawn from the evidence. *Autohaus Brugger, Inc. v. SAAB Motors, Inc.*, 567 F.2d 901, 910-11 (9th Cir.), *cert. denied*, 436 U.S. 946 (1978). If upon the application of this standard of review, the court finds that the evidence supports only one reason-

able conclusion as to the verdict and that conclusion favors the moving party, that party is entitled to the entry of a favorable judgment. *Id.*

DISCUSSION

Defendants have advanced three arguments in support of their motion which may be readily rejected. They contend that the evidence conclusively established that they lacked the requisite intent to commit a Rule 10b-5 violation, that defendants Driscoll, McPhail, and Moore played an insufficient role in connection with their purchase of plaintiff's stock to render themselves liable under the controlling person doctrine of section 20a of the Securities and Exchange Act, 15 U.S.C. § 78t, and that Lindquist failed to make any affirmative misstatements which a jury could have properly construed to be negligent misrepresentations.

On the question of scienter, the Court instructed the jury that in order to establish liability on a Rule 10b-5 claim, plaintiff had the burden of proving by a preponderence of the evidence that each defendant acted towards plaintiff with an intent to deceive, manipulate, or defraud him or with a reckless disregard to the truth or falsity of statements made with respect to facts not disclosed to him. *See generally, Nelson v. Serwold,* 576 F.2d 1332, 1336-37 (9th Cir.), *cert. denied,* 439 U.S. 970 (1978). The jury reasonably could have drawn an inference that each defendant acted with such intent from the evidence indicating defendants' non-disclosure of the events leading up to the merger and Lindquist's alleged comment made in September to Fowler to the effect that Bearing was not then engaged in any merger negotiations. Furthermore, defend-

ants' argument that their testimony indicating that it was their subjective belief in 1977 that Fowler had irrevocably committed himself to sell the stock precluded a finding of the requisite intent on their part carries no weight since the jury was fully entitled to reject this aspect of their testimony. The evidence adduced at trial clearly supports a finding that defendants acted with the requisite scienter.

The evidence also supports the finding that defendants McPhail, Driscoll, and Moore were subject to potential liability herein under the controlling person doctrine of section 20a of the Securities and Exchange Act. Under that section, persons who exercise direct or indirect control over someone who has committed a violation of the Act are liable under the Act to the same extent as the controlled person. The status of these defendants as purchasers of the stock and their authorization of Lindquist to negotiate the terms of the purchase on their behalf constitutes sufficient evidence to support the conclusion that they exercised a high enough "level of participation" in the activities of the controlled person (Lindquist) to expose themselves to liability for his statutory violations. *See generally, Christoffel v. E. F. Hutton & Co., Inc.*, 588 F.2d 665, 668 (9th Cir. 1978).

Insofar as defendants' next argument is concerned, plaintiff's testimony that Lindquist informed him in September that Bearing was not then engaged in any merger negotiations provides sufficient evidence to support the finding that Lindquist committed the tort of negligent misrepresentation. Numerous events, including the inspection trip, which had involved, at least, in a nonlegalistic sense of the word, "negotiations" between Bearing and Genuine Parts,

had occurred prior to this statement. Placed in this context, the jury could have reasonably viewed this comment to be an affirmative misstatement of a material fact actionable under state law as a negligent misrepresentation. *See generally*, 4 Witkin, *Summary of California Law* § 480 (8th ed. 1974). In addition, the fact that Lindquist was not in the business of supplying information does not protect him from liability on this claim. Lindquist has failed to cite any cases in support of this suggested limitation and has also failed to proffer any sound policy arguments in support thereof. His important role in the transaction gave rise to a duty to avoid making a negligent misrepresentation to plaintiff. The Court rejects his contentions on this issue.

Defendants' most vigorously pressed argument in support of their motion, which they have raised at various stages of this litigation, commands much more serious attention than these other contentions. This argument focuses upon the legal significance of the events which transpired at the January 27th meeting. Defendants claim that the evidence supports only the conclusion that at that meeting, plaintiff exercised his option to sell his Bearing stock. This execution of the option then gave rise to the creation of a binding bilateral contract between the parties to that option under the terms of which plaintiff became legally bound to sell his stock to Lindquist or the corporation at the price set in their original written agreement. Once in effect, this commitment, they contend, obligated plaintiff to sell the stock at that price regardless of what information he later acquired about Bearing's merger plans or any other subject. Defendants assert that this fact eliminated

the possibility that subsequent misconduct on their part could have caused him any injury. Plaintiff's failure to show causation, they conclude, establishes as a matter of law their entitlement to an entry of a judgment notwithstanding the verdict.

Defendants have constructed this argument upon a sound legal basis. Hornbook contract law provides that the exercise of an option contract gives rise to a binding bilateral contract between the parties to that option. *See Palo Alto Town & Country Village, Inc. v. BBTC Co.*, 11 Cal. 3d 494, 502, 521 P.2d 1097, 1101, 113 Cal. Rptr. 705, 709 (1974); 1A *Corbin on Contracts* § 264 (1950). In addition, causation is an essential element of a claim based upon Rule 10b-5, *see Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128 (1972), and one based upon the common law tort of negligent misrepresentation. *See* 4 Witkin, *Summary of California Law* § 488. Furthermore, defendants' particular union of these two fundamental principles finds support in the applicable case law. In numerous 10b-5 cases involving similar legal issues and related factual situations, courts have held that the critical date for determination of whether a 10b-5 violation has occurred is the time when the complaining party has become committed to purchase or sell the stock at issue. *See Radiation Dynamics, Inc. v. Goldmuntz*, 464 F.2d 876 (2d Cir. 1972); *Pittsburgh Coke & Chemical Co. v. Bollo*, 421 F. Supp. 908 (E.D.N.Y. 1976), *aff'd.*, 560 F.2d 1089 (2d Cir. 1977); *see generally, The Toledo Trust Co. v. Nye*, 588 F.2d 202 (6th Cir. 1978); *St. Louis Union Trust Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 562 F.2d 1040 (8th Cir. 1977), *cert. denied*, 435 U.S. 925 (1978). The reasoning underlying these cases,

which is equally pertinent to a claim based upon negligent misrepresentation, is that a failure to inform a party to a binding contractual obligation of a material fact that he would probably act upon were he not committed to act otherwise does not cause that party legally recognized injury. His theoretical inability to alter his actions prevents the other party's conduct from having a legal effect.

While plaintiff apparently accepts in theory the legitimacy of this causation argument, he does dispute defendants' version of the factual events and the legal consequences of the January meeting. Plaintiff denies that he exercised his option at that meeting and argues that even if he had intended to exercise it, his failure to comply with the time and method provisions set out in the parties' initial written agreement would have rendered such an attempt inoperable. Plaintiff claims that the parties first entered a legally binding agreement upon the signing of the final written contract on November 4, 1977. He properly contends that the absence of an earlier commitment would thwart defendants' causation argument.

The resolution of this issue thus depends upon whether a reasonable jury could have concluded from the evidence in the record that plaintiff did not exercise his option or whether the exercise of that option, if it was attempted, was invalid as a matter of law. Plaintiff's deposition and trial testimony and the other evidence presented at trial lead inescapingly (sic) to the conclusion that he did, in fact, exercise a legally valid option.

Both at trial and at deposition, plaintiff essentially admitted that he exercised the option. His recollection of what

he stated at the January meeting differs in significant respects from his counsel's characterization of that testimony and, therefore, it is incumbent upon the Court to scrutinize closely his actual statements.

The central thrust of his testimony, corroborated by defendants' testimony, was that once Lindquist informed him at the meeting that Bearing was not then engaged in any merger negotiations, he unequivocally offered his stock for sale. The following portion of the transcript of his cross examination represents a fair sample of his testimony on this subject:

Q. Now at the meeting, you met at the company, didn't you, on January 27th?

A. I presume so.

Q. Do you recall who was present?

A. Unless there are notes on it—no, I presume Mr. Blascka (sic) and Mr. Lindquist.

Q. And yourself.

A. Right.

Q. And was it in Mr. Lindquist's office?

A. I would say yes.

Q. Okay. What did he say on the subject of your option?

A. Well, I believe that he started right off and said, "Now, remember, you don't have to sell any of this, but you do have a liquidity position to think about, and one thing I can tell you is I'm not in negotiations for the sale of this." I can't say that it went beyond that.

Q. What did you say?

A. I can't say that it went beyond that. I can't say what else he said.

Q. And then you said something, right?

A. Well, yes, I guess so.

Q. And what did you say?

A. I probably said that I would sell the shares of stock. Yes.

Q. All right. And you didn't have any conditions on that you just said, "I will sell."

A. I would if I had the conditions that Mr. Lindquist just spoke about.

Q. He said that?

A. Yes.

Q. And you said, "I will sell my stock"; right?

A. Under those conditions. I didn't add those conditions but I didn't feel it was necessary because he already explained that he was not having any negotiations. Now, I accepted that.

Q. But you just said, "I will sell my stock."

A. Yes.

. . . .

Q. But, nevertheless, you decided to sell your stock in January?

A. No, Mr. Parkinson. You're getting the timing wrong, I think.

My decision to sell the stock in January was based on the fact that I was told there were no negotiations going on.

Q. All right. You had been told that, and you decided to sell?

A. Right.

Q. But this was even though you thought the price would go up if there was a merger some day?

A. Oh, yes; certainly I'll accept that.

Transcript, Cross Examination of Charles A. Fowler at 17-18, 22.

In this testimony, plaintiff admits, contrary to his counsel's assertions, that he did not add any conditions to the terms of the proposed sale.

This testimony leaves little room for any conclusion but that plaintiff decided that in view of the then-dormant status of Bearing's merger possibilities he would take advantage of his option and sell the stock to the corporation. In view of the unqualified nature of his offer to sell and the circumstances and purpose of the meeting, a reasonable person could only have viewed the words with which he communicated his intent to Lindquist and Blaschka as his acceptance of the offer found in the option.

The parties' conduct after this meeting further substantiates the conclusion that plaintiff thusly exercised his option. Their subsequent actions suggest that they shared a common belief that the events of January 27th had left them obligated to complete the transaction pursuant to the terms of the written agreement. Bearing immediately after the meeting commenced its monthly payments to plaintiff, thereby evidencing its ultimate obligation to purchase the stock. Two weeks after the meeting, Lindquist informed plaintiff that he would not personally purchase the stock as he was entitled to do under the written agreement. Discussions concerning the substitution of the parties and the method of computing the price to be paid for the stock serve as additional indicators that the parties considered themselves bound by the terms of the agreement and that they believed they could only change those terms by gaining the consent of the other party. Accordingly, plaintiff initially sought to wrest more favorable terms from the proposed new purchasers in exchange for his consent sanctioning their substitution. These considerations viewed in conjunction with plaintiff's admissions compel the conclusion that plaintiff exercised his option.

Plaintiff's arguments that evidence in the record supports the conclusion that he did not exercise his option fall under the weight of his own admissions. As noted above, plaintiff's testimony directly conflicts with his counsel's assertions that plaintiff conditioned his offer to sell the stock to the corporation upon the right to retain the stock if Bearing entered merger negotiations prior to the finalization of the sale.* Plaintiff's stated concern was with Bearing's "present" merger status, not future events. Having received reassurance from Lindquist on this subject, plaintiff then unambiguously manifested his assent to the

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*In support of his characterizations of plaintiff's testimony, counsel referred the Court to only one passage in the transcript. The following exchange occurred on counsel's redirect examination of plaintiff:

> Q. At this meeting (in September) you were told you could change your mind with respect to the sale of stock; is that your testimony?
>
> A. I don't say it was said: You can change your mind about the sale of the stock—I mean in those words exactly. But I think Mr. Lindquist said something like: Remember you don't have to actually sell that stock, but remember your liquidity position, and I'm not presently negotiating with anyone for the sale or purchase of the company.

Transcript of Redirect Examination of Charles A. Fowler at 4. This testimony, however, carries little weight due to its inherent ambiguities, direct conflicts with plaintiff's other testimony, the vagueness of plaintiff's recollection, and the leading nature of counsel's question. Furthermore, in view of the other evidence in the case conclusively establishing plaintiff's exercise of his option—and this particular testimony clearly does not directly bear upon that issue—this statement could only suggest the unlikely possibility that defendants would have agreed to a mutual recission (sic) of the contract if plaintiff had so requested. Plaintiff's failure to argue this weak theory to the Court or the jury, however, keeps it out of the case.

offer. Whatever unstated reservations or subjective understanding of his obligations he may have held on this subject would not affect the objective legal consequences of his actions. In addition, evidence of the discussions between the parties and the deviations in the final contract cannot, standing alone and against plaintiff's testimony, support the conclusion that plaintiff failed to exercise his option. In the context in which these events occurred, this evidence simply indicates that the parties exercised their rights to discuss and agree to a novation and a consensual modification of the contract. *See* Cal. Civ. Code §§ 1530 and 1531 (West 1954); *see generally, The Toledo Trust Co. v. Nye*, 588 F.2d at 206; *Pittsburgh Coke & Chemical Co. v. Bollo*, 421 F. Supp. at 923.

The evidence adduced at trial also established that plaintiff's exercise of the option was legally valid. Plaintiff argues that his noncompliance with the terms of the initial agreement requiring acceptance of the option in writing and within 20 days of his retirement automatically extinguished the option and thus left the parties without a binding agreement until November.

This conclusion, however, finds plaintiff in the position of invoking for his benefit contractual provisions presumably inserted in the contract for the benefit of the offeror. Traditional tenets of contract law view provisions controlling the method of acceptance as intended for the benefit of the offeror and permit the offeror to waive compliance with these provisions. *See, e.g., Artukovich v. Pacific States Cast Iron Pipe Co.*, 78 Cal. App. 2d 1, 3, 176 P.2d 962, 964 (2d Dist. 1947). This rule derives from the

fact that an offeree will usually be unable to show that his own failure to accept an offer in a contractually specified manner will cause him any prejudice. The rule applies with equal effect to the exercise of an option. *See Collins v. Marvel Land Co.*, 13 Cal. App. 3d 34, 40, 91 Cal. Rptr. 291, 294 (2d Dist. 1970); *Alpern v. Mayfair Markets*, 118 Cal. App. 2d 541, 547, 258 P.2d 7, 10 (2d Dist. 1953); 1A *Corbin on Contracts*, § 273 at 594. Defendants herein thus had the right to excuse plaintiff from complying with the contract provisions governing the manner in which he exercised the option.

The issue of waiver ordinarily would raise a factual question for jury determination. The evidence presented in this trial, however, supports only the conclusion that defendants waived plaintiff's noncompliance; if the jury found otherwise, the Court must reject that finding.

A waiver may be communicated either through an express statement to that effect or through a course of conduct which in the applicable circumstances conclusively indicates the waiving party's intentions. *Alpern v. Mayfair Markets*, 118 Cal. App. 2d at 547, 258 P.2d at 10. Defendants' conduct herein unequivocally communicated a waiver. Lindquist's role in arranging the initial meeting strongly suggests a lack of concern over plaintiff's strict compliance with the time provisions. That Fowler's vacation trip to Hawaii may have been a contributing factor to the lateness of the exercise of his option further corroborates the suggestion that defendants had such an attitude on this subject because Bearing helped pay for the trip and thus rendered it more difficult for plaintiff to

make a timely exercise of his option. In addition, plaintiff's exercise of the option was only seven days late. Defendants' actions after the meeting, including the commencement of the monthly payments to plaintiff and the nature and content of their discussions with him, demonstrate their acceptance of the corporation's obligation to purchase the stock. Their unwaivering adherence to this obligation implicitly signified their acceptance of plaintiff's method of exercising his option. This evidence considered in conjunction with the absence of any serious conflicting evidence on this question compels the Court to reach the conclusion that defendants excused plaintiff from compliance with these provisions.

Having determined that the evidence supports only the conclusions that plaintiff exercised a legally valid option, that defendants accepted plaintiff's method of exercising the option, and that these actions committed plaintiff to a future course of conduct which he was not free to alter, the Court must find that defendants' alleged misconduct occurred too late in the events to cause plaintiff any legal injury. Therefore, the Court grants defendants' motion for a judgment notwithstanding the verdict.

MOTION FOR A NEW TRIAL

Defendants have moved, in the alternative, for a new trial. On a motion for a new trial, the Court may reweigh the evidence and set aside the verdict if it concludes that the verdict is against the clear weight of the evidence. 6A *Moore's Federal Practice* ¶ 59-08[5] (rev. ed. 1976). The discussion above adequately substantiates the Court's determination that the verdict in this case conflicted with

the clear weight of the evidence. In the absence of the entry of the judgment notwithstanding the verdict, the Court would have granted defendants' motion for a new trial.

Accordingly, It Is Hereby Ordered that defendants' motion for a judgment notwithstanding the verdict is GRANTED in favor of each of the defendants and that judgment shall be entered herewith.

Dated: June 11, 1980.

/s/ ALBERT C. WOLLENBERG
United States District Judge

APPENDIX B

United States Court of Appeals
For the Ninth Circuit

No. 80-4332
DC # C78-1190

Charles A. Fowler,
Plaintiff-Appellant,

vs.

Bearing Specialty Company, a corporation;
R. E. Lindquist, Robert W. Blaschka,
Norman D. McPhall (sic), Roy T. Driscoll, John Moore,
Defendants-Appellees.

MEMORANDUM

[Filed Jan. 22, 1982]

Appeal from the United States District Court
for the Northern District of California
Albert C. Wollenberg, District Judge, Presiding
Argued and Submitted December 15, 1981

Before: SNEED, and BOOCHEVER, Circuit Judges,
and TAKASUGI*, District Judge

Appellant brought suit against the Bearing Specialty Company [Bearing] and its corporate officers alleging violation of federal securities law, 15 U.S.C. § 78j(b), 15

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*Honorable Robert M. Takasugi, United States District Judge for the Central District of California, sitting by designation.

U.S.C. § 78t, and 17 C.F.R. § 240.10b-5 (rule 10b-5), common law fraud, and negligent misrepresentation. Specifically, appellant alleged that appellee Lindquist, a Bearing officer, knowingly gave him various information stating that Bearing was *not* involved in merger negotiations, and thereby induced him to sell his Bearing stock. Bearing's other officers are named as defendants under the "controlling person" doctrine, *see* 15 U.S.C. § 78t. Appellant asserted that he incurred damages because, subsequent to his sale of Bearing stock, Bearing's merger with another corporation caused its stock to appreciate in value by $6.50 per share. Appellees responded by contending that appellant agreed to sell his stock prior to any alleged misrepresentation and that any misconduct subsequent to this agreement could not have caused him injury.

At trial the court dismissed the claims against Bearing, and, in due course, the case was submitted to the jury which returned a verdict against the remaining appellees. Following this verdict the appellees moved for a JNOV. The trial court granted this motion on the ground that the facts conclusively established that the appellant agreed to sell his stock in January, 1977. As a result, the alleged misrepresentations could not have caused injury to the appellant. We reverse and remand with directions to enter judgment against all of the appellees other than Bearing in accordance with the jury verdict.

The standard of review in determining whether to overturn the entry of JNOV has recently been restated in

William Inglis, etc. v. ITT Continental Baking Co., 652 F.2d 917 (9th Cir. 1981).

> "That is, we must affirm the district court if, without accounting for the credibility of the witnesses, we find that the evidence and its inferences, considered as a whole and viewed in a light most favorable to the non-moving party can support only one reasonable conclusion—that the moving party is entitled to judgment notwithstanding the adverse verdict."

Id. at 930. We have reviewed the complete record of this case, including the Reporter's Transcript, and we cannot say that the evidence and its inferences reasonably can support only the conclusions accorded it by the district court.

We hasten to point out that we have no quarrel with certain of the district court's conclusions. That is, we agree that the "jury reasonably could have drawn the inference that each defendant acted with such intent [that intent necessary to establish liability under Rule 10b-5] from the evidence indicating defendants' non-disclosure of the events leading up to the merger and Lindquist's alleged comment made in September to Fowler to the effect that Bearing was not then engaged in any merger negotiations." We also agree that the liability of appellees Driscoll, McPhail and Moore under the controlling person doctrine of the securities law is supported by the evidence. The district court is also correct in holding that sufficient evidence exists to support the jury's finding that appellee Lindquist committed the tort of negligent misrepresentation by representing that merger negotiations were not underway in September, 1977.

However the district court erred in holding that the jury could not reasonably find that the appellees' misconduct caused the appellant's injury. Our review of the record convinces us to the contrary. The position of the district court is based on the proposition that the appellant became obligated to sell his stock to the Bearing Specialty Company on January 27, 1977. On that date he exercised his option to sell with the result that a bilateral contract to sell and purchase arose between appellant and Bearing. *See Palo Alto Town & Country Village, Inc. v. BBTC Co.*, 11 Cal.3d 494, 502, 521 P.2d 1097, 1101, 113 Cal. Rptr. 705, 709 (1974); 1A *Corbin on Contracts* § 264 (1963).

Appellee, however, stoutly maintained throughout the trial that he did not exercise his option. His basic position, which he repeated several times during his testimony, was that his "offer to sell" the shares in the January 27, 1977 meeting was conditioned on there being no present negotiations looking to a merger of Bearing with another company and that appellee Lindquist recognized on several occasions that, while Bearing under the option contract was obligated to buy appellant's stock, appellant was not obligated to sell until November, 1977.

Appellee's version, which is supported by reasonable inferences that can be shown from the testimony of his attorney estate planner, is not inconsistent with the evidence concerning the events that occurred subsequent to January 27, 1977. This evidence, *inter alia*, tends to show that Lindquist did not wish to have Bearing make the purchase and that he preferred that the shares be purchased by the other appellees directly from appellant. During the course of

negotiations differences arose regarding the rate of interest to be paid on the deferred purchase price, the manner in which the stock was to be valued, and the number of shares to be retained by the appellant for sale to his son. While these differences are also not inconsistent with the appellees' contentions that the appellant exercised his option on January 27, 1977 and that subsequent negotiations sought to achieve a novation, their compatibility with both the appellant's and appellees' theory of the case underscores the correctness of refusing to conclude that the jury could reach but one reasonable conclusion.

The district court's conclusion that the jury reasonably only could find that the appellant exercised his option to sell on January 27, 1977, rests almost entirely on appellant's testimony on cross-examination that he had said on that date that "I will sell any stock." R.T. Vol. III, pp. 17-18. In view of the appellant's understanding of these words and the context in which they were spoken, it cannot be said that a jury could not reasonably find that appellee Lindquist also did in fact so understand them and that such understanding was reasonable. 3 *Corbin on Contracts* § 599 (1963). Even appellees' counsel in his final argument to the jury recognized that the issue whether the option had been exercised on January 27, 1977 was one of credibility. He argued:

> "I said the issue is going to be credibility between Mr. Fowler on the one side and Mr. Lindquist and Blaschka on the other hand.
>
> I think, actually, Mr. Fowler has pretty much admitted our case. At other times he denied it. He is every which way, really, but I hope that you will re-

member the times that he would agree with me that he did exercise that option." R.T. Vol. VII, p. 556.

The jury rejected this view of the evidence. We cannot say this rejection was a conclusion which no reasonable jury could reach.

It remains only to point out that appellant's version of the facts that was accepted by the jury does not contravene accepted principles of contract law. In essence, appellant contended thaat the stock purchase agreement gave him an option to sell his stock to either Bearing or appellee Lindquist, which was binding on Bearing when Lindquist elected not to purchase throughout the relevant period of 1977. This option was supported by consideration furnished by appellant at the time he merged his company with Bearing four years previously. The negotiations that commenced on January 27, 1977 amounted to various counter offers put forward by both appellant and appellees which did not terminate appellant's power to accept the option should he have chosen to do so. *See Hayward Lumber & Investment Co. v. Construction Products Corp.*, 255 P.2d 473, 117 Cal.App.2d 221 (1953); 1 *Corbin on Contracts* § 91 (1963). Bearing and Lindquist previously had waived the requirement that appellant exercise his option in writing within twenty days of his retirement. Appellees admit this waiver occurred and the jury also must have so found. The charge given to the jury relevant to the option adequately expresses these principles of contract law.

One final matter requires attention. The district court indicated tl[illegible] in the absence of the entry of the JNOV it would have granted the defendants' motion for a new

trial. Although its remark could have been more explicit, we here treat its remark as a conditional grant of a new trial. We reverse this conditional grant of a new trial because we are convinced that "there is no valid useful purpose for submitting the case to another jury." *Fireman's Fund Insurance Co. v. AALCO Wrecking Co.*, 466 F.2d 179, 187 (8th Cir. 1972). We therefore reverse and remand with directions to enter judgment against all of the appellees other than Bearing in accordance with the jury verdict.

REVERSED AND REMANDED.

APPENDIX C

United States Court of Appeals
For the Ninth Circuit

No. 80-4332

Charles A. Fowler,
Plaintiff-Appellant,

vs.

Bearing Specialty Company, a corporation;
R. E. Lindquist, Robert W. Blaschka,
Norman D. McPhail, Roy T. Driscoll, John Moore,
Defendants-Appellees.

ORDER

[Filed March 1, 1982]

Before: SNEED, and BOOCHEVER, Circuit Judges,
and TAKASUGI*, District Judge

Defendant-Appellees' petition for rehearing and modification of reversal of conditional grant of new trial pursuant to Rule 40, Federal Rules of Appellate Procedure is denied.

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*Honorable Robert M. Takasugi, United States District Judge for the Central District of California, sitting by designation.

APPENDIX D

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United States Court of Appeals
For the Ninth Circuit

No. 80-4332

Charles A. Fowler,
Plaintiff,

vs.

Bearing Specialty Company, a corporation;
R. E. Lindquist, Robert W. Blaschka,
Norman D. McPhail, Roy T. Driscoll, John Moore,
Defendants.

Petition for Rehearing and Modification of
Reversal of Conditional Grant of New Trial
Pursuant to Rule 40, Federal Rules of Appellate Procedure

TO THE CLERK OF THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT:

I

INTRODUCTION

The Court has reversed both the JNOV and conditional grant of new trial which had been ordered by Judge

Wollenberg. Defendants/respondents move the Court for a rehearing of the portion of its order reversing the grant of new trial, and seek a modification directing a new trial confined to the issues 1) whether or not plaintiff exercised his option in January 1977, and, if so, 2) whether or not in doing so the 1973 option contract between the parties was modified. On such a new trial, defendants/respondents would concede that if plaintiff did not so exercise his option or if in doing so, he reserved a right to rescind, defendants/ respondents are liable to plaintiff in the amount of the previous verdict.

II

STATEMENT OF COUNSEL

In the judgment of the undersigned counsel for defendants/respondents, the Court in its decision has overlooked a material point of law on the grant of a new trial: that under the Supreme Court and Ninth Circuit doctrine, a grant of new trial will not be reversed unless its grant constituted a clear abuse of the Trial Court's discretion. Furthermore, in the judgment of counsel, the reversal of the grant of new trial creates apparent conflicts with other decisions of this Court which are not addressed in the Court's Memorandum.

III

THE COURT HAS DISREGARDED ESTABLISHED PRECEDENT IN HOLDING THAT NO VALID USEFUL PURPOSE WOULD BE SERVED BY RESUBMITTING THE CASE TO A JURY, ALTHOUGH THE TRIAL JUDGE DISCREDITED THE ONLY EVIDENCE SUPPORTING PLAINTIFF'S POSITION

A. Plaintiff's testimony which the Trial Court discredited was the only evidence that Lindquist shared plaintiff's unspoken understanding that he had a right to rescind

This Court has reversed the JNOV because of plaintiff's testimony that appellee Lindquist recognized on several occasions that plaintiff had reserved a right to rescind the exercise of his option to sell his stock if the company should subsequently enter into merger negotiations. Plaintiff's testimony is the only evidence that Lindquist had such an understanding. Yet the Trial Court discredited that testimony by plaintiff, both in granting judgment NOV and new trial. Judge Wollenberg held that the clear weight of the evidence was to the contrary (excerpts, pp. 153, 156). Although this Court's opinion found some support for plaintiff's testimony on the basis of inferences from his attorney's testimony, only plaintiff's testimony supports an inference that Lindquist shared an unexpressed understanding with plaintiff that he had exercised his option subject to a right to rescind subsequently. It is significant that this Court did not dispute the Trial Court's finding that the clear weight of the evidence was to the contrary. And indeed the clear weight of the evidence was

to the contrary. The terms of the written contract contained no condition (Ex. A). Mr. Fowler admitted there was no condition stated (tr. pp. 84-86). Lindquist denied ever making a statement at any time after Fowler exercised his option that Fowler had a right to rescind (tr. pp. 347-348). The condition subsequent found by the Court makes the corporate decision to commence payments to plaintiff immediately after he exercised his option a rash one, to say the least (tr. pp. 87, 108-114, 54-56).

B. This Court's reversal of the conditional new trial order departs from precedent in holding that a new trial would serve no purpose despite the Trial Court's unchallenged finding that the clear weight of the evidence was to the contrary

The Supreme Court has consistently held that the authority to grant a new trial is almost entirely discretionary with the Trial Court. *Montgomery Ward & Co. v. Duncan*, 311 U.S. 243, 251, 61 S.Ct. 189, 194 (1940); *Neely v. Martin K. Ely Construction Company*, 386 U.S. 317, 325, 87 S.Ct. 1072, 1078 (1967) (emphasizing "the trial judge's first-hand knowledge of witnesses, testimony and issues . . . his 'feel' for the overall case.")

The most recent affirmation of this doctrine by the Supreme Court which we could find is in *Allied Chemical Corp. v. Daiflon, Inc.*, 449 U.S. 33, 101 S.Ct. 188, 191 (1980), in which the Supreme Court reversed a grant of mandamus by the Court of Appeals which had directed the Trial Court to restore in part a jury verdict after the Trial Court had granted new trial. The Court held:

"The authority to grant a new trial, moreover, is confided almost entirely to the exercise of discretion on the part of the trial court."

The Ninth Circuit has consistently followed the doctrine that a Trial Court's discretion to grant a new trial will not be reversed except for clear abuse of discretion. *Fount-Wip, Inc. v. Reddi-Wip, Inc.*, 568 F.2d 1296, 1362 (9th Cir. 1978); *Moist Cold Refrigerator Co. v. Lou Johnson Co.*, 249 F.2d 246, 256 (9th Cir. 1957) (duty of trial court to apply weight of evidence rule); *Hanson v. Shell Oil Co.*, 541 F.2d 1352, 1359 (1976) (reversal only for abuse of discretion).

C. The authority cited for reversal of the new trial order because new trial would serve no useful purpose is inapplicable to this factual situation where the clear weight of the evidence is contrary to the verdict

The sole authority which this Court has cited for reversal of the new trial order is *Fireman's Fund Insurance Co. v. Aalco Wrecking Co., Inc.*, 466 F.2d 179 (8th Cir. 1972.) The dissent on denial of petition for hearing in banc in that case pointed out that the *Fireman's Fund* opinion ignored the teachings of the Supreme Court and departed from the Eighth Circuit rule that a new trial order will not be reversed except for clear abuse of discretion (466 F.2d at 188-190).

Yet in *Fireman's Fund*, the Appeals Court, unlike this Court, found that the jury verdict was supported by a variety of uncontroverted evidential factors (466 F.2d at 184). Unlike this Court, in *Fireman's Fund* the Court of Appeals held that, "(a)s to the evidence within the record,

there exists no significant weight factor favoring the defendant."

We submit that it constitutes an extension of the holding of *Fireman's Fund* to apply it to this case in which the testimony discredited by the Trial Court was hotly controverted and contradicted by other clear evidence.

D. It cannot properly be said that a new trial on the limited issues we request would serve no useful purpose.

We request herein that the Court's order be modified to affirm the new trial order only as to the issues of whether plaintiff exercised his option, and if so, the terms of his exercise. We would concede that if he had not exercised his option in January, or if he exercised it by reserving a right to rescind, defendants shall be liable in accordance with the existing verdict. We believe that a new trial so limited will avoid the difficult problem of evaluating evidence which the jury faced in the trial that was had: most of the trial was devoted to other evidence than that concerning the crucial issue of the exercise of plaintiff's option. Thus there was extensive testimony of various contacts with executives of the company which eventually purchased the stock of Bearing Specialty Co. Such a partial retrial is a permissible procedure (*United States ex rel. Greenhalgh v. F.D. Rich Co., Inc.*, 520 F.2d 886, 889 (9th Cir., 1975)).

It cannot properly be said that a trial of issues on which Judge Wollenberg discredited plaintiff's testimony would have no useful purpose.

IV

CONCLUSION

We request that this Court modify its order reversing the new trial order by instead directing a new trial of the issues 1) whether plaintiff exercised his option in January 1977 and, if so, 2) the terms of the agreement which resulted from that exercise.

Dated: February 5, 1982

Respectfully submitted,

ACKERMAN, JOHNSTON, CAMPBELL & PARKINSON

By /s/ BENJAMIN H. PARKINSON
Attorneys for
Defendants/Respondents